

Angeline Hulsen

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OIL AND GAS LEASE
(Paid-Up Lease)

This Oil and Gas Lease (this "Lease") is made on the 5 day of Aug, 2008 between **Houghton Properties, Ltd.**, a Texas limited partnership (hereafter called "Lessor," whether one or more), whose address is **16475 Dallas Pkwy Ste 300 Addison TX 75001** and **Vargas Energy, Ltd.** (hereafter called "Lessee"), whose address is **4200 S. Hulen, Suite 614, Fort Worth, Texas, 76109**.

1. **Grant.** In consideration of Ten Dollars and other consideration in hand paid, Lessor grants and leases exclusively unto Lessee the following described land (the "Land") in Tarrant County, Texas, for the sole purpose of exploring under, drilling under, and producing oil and gas, to produce, save, treat, process, store, and transport oil and gas and other products manufactured from oil and gas produced from the Land:

Lot 1R and Lot 2R, Block 1 of the Riverpark Addition, an Addition to the City of Fort Worth, Tarrant County, Texas, according to the Plat or Replat thereof recorded on June 8, 2007 in Cabinet A, Slide 11977 of the Map or Plat Records of Tarrant County, Texas.

2. **Primary Term.** This Lease is for a term of three (3) years from this date (called "Primary Term") and as long thereafter as oil or gas is produced in paying quantities from the Land or land pooled therewith or this lease is otherwise maintained in effect pursuant to the provisions hereof. The bonus consideration paid by Lessee for this lease shall be paid to Lessor at the address shown above at the time of Lessor's signing and tendering this Lease to Lessee. If Lessee does not commence the drilling of an actual well from a drilling platform erected on lands pooled therewith with a drill bit entering the surface of the earth within the Primary Term then this Lease shall terminate.

3. **Minerals Covered.** This Lease covers only oil and gas. The term "oil and gas" means oil, gas, and other liquid and gaseous hydrocarbons produced through a well bore.

4. **Royalty.**

(a) As royalties, Lessee agrees:

(1) To deliver free of cost to Lessor at the wells or to the credit of Lessor at the pipeline to which the wells may be connected, one-fourth (1/4) (the "Royalty Fraction") of all oil and other liquid hydrocarbons produced and saved from the Land. At Lessor's option, which may be exercised from time to time, Lessee shall pay to Lessor the same part of the market value at the well of oil and other liquid hydrocarbons of like grade and gravity prevailing on the day the oil and other hydrocarbons are run from the Lease in the general area in which the Land is located.

(2) To pay to Lessor:

(i) On gas produced from the Land and sold by Lessee or used off the Land and to which the following subparagraphs (ii) and (iii) do not apply, the Royalty Fraction of the greater of either the market value or gross proceeds received by Lessee at the point of sale, use, or other disposition.

(ii) On gas produced from the Land that is processed in a processing plant in which Lessee or an affiliate of Lessee has a direct or indirect interest, the higher of the Royalty Fraction of the market value of the gas at the inlet to the processing plant, or the Royalty Fraction of the market value of all processed liquids saved from the gas at the plant plus the Royalty Fraction of the market value of all residue gas at the point of sale, use, or other disposition.

(iii) On gas produced from the Land that is processed in facilities other than a processing plant in which Lessee or an affiliate of Lessee has a direct or indirect interest, the Royalty Fraction of the gross proceeds received by Lessee at the plant of all processed liquids credited to the account of Lessee and attributable to the gas plus the Royalty Fraction of the gross proceeds received by Lessee of all residue gas at the point of sale, use, or other disposition.

(b) If gas produced from the Land is sold by Lessee pursuant to an arms-length contract with a purchaser that is not an affiliate of Lessee, and for a term no longer than that which is usual and customary in the industry at the time the contract is made, then the market value of the gas sold pursuant to the contract shall be the total proceeds received by Lessee in the sale, subject to the provisions of paragraph 4(c) below.

(c) The market value of gas will be determined at the specified location by reference to the gross heating value (measured in British thermal units) and quality of the gas. The market value used in the calculation of oil and gas royalty will never be less than the total proceeds received by Lessee in connection with the sale, use, or other disposition the oil or gas produced or sold. For purposes of this paragraph, if Lessee receives from a purchaser of oil or gas any reimbursement for all or any part of severance or production taxes, or if Lessee realizes proceeds of production after deduction for any expense of production, gathering, dehydration, separation, compression, transportation, treatment, processing, storage, or marketing, then the reimbursement or the deductions will be added to the total proceeds received by Lessee. Royalty will be payable on oil and gas produced from the Land and consumed by Lessee on the Land for compression, dehydration, fuel, or other use.

(d) Unless specified herein, Lessor's royalty may not be charged, directly or indirectly, with any of Lessee's expenses of production, gathering, compressing, treating or marketing the oil and gas produced from the Land, and all of such expenses shall be considered costs of production and not post production costs. Royalty will be paid on gas used by Lessee in compression, but royalties will not be paid on gas used in gas lift operations or recycling. It is the intent of the parties that the provisions of this Section 4(d) are to be fully effective and enforceable and are not to be construed as "surplusage" under the principles set forth in *Heritage Resources v. NationsBank*, 939 S.W.2d 118 (Tex. 1997). Notwithstanding the foregoing, Lessor's royalty may be charged with costs and expenses of transporting, dehydrating, compressing, processing and treating gas produced from the lease as long as such costs are charged to Lessee by a gas purchaser or transportation company which is not an affiliate of Lessee in an arms length transaction, and provided such costs do not exceed those charged for performing similar services by unrelated third parties in arms length transactions in Tarrant County, Texas. If gas produced from the Land is sold by Lessee pursuant to an arms-length contract with a purchaser that is not an affiliate of Lessee, and for a term no longer than that which is usual and customary in the industry at the time the contract is made, then the market value of the gas sold pursuant to the contract shall be the total proceeds received by Lessee in the sale. Lessor's royalty will never bear, either directly or indirectly, any part of the costs or expenses of production, separation, gathering, dehydration, compression, transportation, trucking, processing, treatment, storage, or marketing of the oil or gas produced from the Land or any part of the costs of construction, operation, or depreciation of any plant or other facilities or equipment used in the handling of oil or gas. However any such costs which result in enhancing the value of the marketable oil, gas or other products to receive a better price may be deducted from Lessor's share of production so long as they are based upon Lessee's actual costs of such enhancements.

(e) Lessor shall be paid the Royalty Fraction of all payments and other benefits made under any oil or gas sales contract or other arrangement, including take-or-pay payments and payments received in settlement of disputes; provided that if Lessor receives a take-or-pay payment or similar payment for gas that has not been produced, and if the gas is subsequently produced, Lessor will only receive its Royalty Fraction of any payments made for make-up gas taken pursuant to the take or-pay provision or similar provision.

(f) Lessee must disburse or cause to be disbursed to Lessor its royalty on production from a particular well not later than 120 days after completion of the well, in the case of an oil well, or after the pipeline connection, in the case of a gas well. Thereafter, Lessee must disburse or cause to be disbursed to Lessor its royalty on production by the last day of the second month after the month of production. If not paid when due, Lessor's royalty will bear interest at the maximum lawful rate from due date until paid, which amount Lessee agrees to pay. Acceptance by Lessor of royalties that are past due will not act as a waiver or estoppel of its right to receive interest due thereon unless Lessor expressly so provides in writing signed by Lessor. The royalty payment obligations under this

Lease shall not be affected by any division order or the provisions of the Section 91.402 of the Texas Natural Resources Code or any similar statute. Should Lessee fail at any time to pay royalty when due, Lessor may give Lessee written notice of the default, and if the default is not cured within 60 days of the notice of the default, Lessor shall have, in addition to all other remedies, the right to terminate this Lease.

(g) As used in this Lease, "affiliate" means (i) a corporation, joint venture, partnership, or other entity that owns more than ten percent of the outstanding voting interest of Lessee or in which Lessee owns more than ten percent of the outstanding voting interest; or (ii) a corporation, joint venture, partnership, or other entity in which, together with Lessee, more than ten percent of the outstanding voting interests of both Lessee and the other corporation, joint venture, partnership, or other entity is owned or controlled by the same persons or group of persons.

(h) The receipt by Lessee from a purchaser or a pipeline company of proceeds of production for distribution to Lessor will not result in Lessee acquiring legal or equitable title to those proceeds, but Lessee will at all time hold the proceeds in trust for the benefit of Lessor.

5. **Shut-in Royalty.** While there is a gas well on this Lease or on acreage pooled therewith capable of producing gas in paying quantities, but gas is not being sold, Lessee shall pay or tender in advance an annual shut-in royalty of \$50.00 per acre for each well on or under the Land or wells holding this Lease by pooling. Payment will be due within 60 days after the well is shut-in. While shut-in royalty payments are timely and properly paid, this Lease will be held as a producing lease. After the expiration of the primary term of this lease, the right of Lessee to maintain this Lease in force by payment of shut-in gas royalty is limited to an aggregate period of two (2) years. The obligation of Lessee to pay shut-in royalty is a condition and not a covenant. The payment or tender of royalty under this paragraph may be made by the check of Lessee mailed or delivered to the parties entitled thereto on or before the due date.

6. **Continuous Development.**

(a) If, at the expiration of the Primary Term, oil or gas is not being produced from the Land, but Lessee has commenced the actual drilling of a well under the Land or on other lands pooled therewith, the Lease will not terminate but will remain in effect for so long thereafter as actual operations with respect to such well are carried out with due diligence with no cessation of more than 90 days, and if such the operations result in the production of oil or gas, the Lease shall remain in force and effect as otherwise provided herein. For the purposes of this Lease, the term "operations" means operations for any of the following: actual drilling, testing, completing, reworking, recompleting, deepening, plugging back, or repairing of a well in search for or in an endeavor to obtain production of oil or gas on a drill site tract with which the Land is pooled.

(b) If this Lease is maintained beyond the expiration of the Primary Term by production or otherwise, it will remain in force as to all acreage and depths as long as there is no lapse of more than 180 days between the completion of one well and the commencement of the actual drilling of another well on a drill site tract with which the Land is pooled. The commencement of actual drilling means the penetration of the surface of a drill site tract with which the Land is pooled with a drilling rig capable of drilling to the anticipated total depth of the well. After a well is commenced, drilling operations must continue in a good and workmanlike manner in a good faith effort to reach the anticipated total depth with no cessation of operations for more than 90 consecutive days. The permitted time between wells shall be cumulative so that if a well is commenced prior to the date it is required to be commenced, the number of days prior to the date on which the well should have been commenced shall be added to the time permitted for the next succeeding well. Upon receipt of a written request from Lessor, Lessee shall within one hundred eighty (180) calendar days provide Lessor with a written computation of the dates relevant to this subparagraph and the supporting documentation therefore.

(c) If at any time the maximum time for the commencement of the actual drilling of a well expires without such commencement having occurred, or upon the expiration of the Primary Term if the Lease is not maintained by continuous drilling, the Lease will then terminate as to all depths 100 feet below the base of the Barnett Shale Formation in a well then producing on such Subject Lands. If production in paying quantities from the Subject Lands ceases from any cause, this Lease will terminate as to that the Subject Lands unless Lessee commences operations

for drilling or reworking on a drill site tract with which the Land is pooled within 180 days after the cessation of production, in which case the Lease as to that the Subject Lands will continue in force as long as the operations are prosecuted with due diligence with no cessation of more than 90 consecutive days, and if such operations result in production, so long thereafter as there is production in paying quantities from such Subject Lands.

(d) As used in this Lease, the term "horizontal well" means a well that meets the definition of a "horizontal drainhole well" under Statewide Rule 86 of the Railroad Commission of Texas, and a "vertical well" is a well that is not a horizontal well.

(e) Nothing in this paragraph 6 shall be construed as granting Lessee access to the surface of the Land for any purpose.

7. **Pooling.** Lessor and Lessee recognize that it may in the interest of each party for the Land to be pooled/unitized with adjacent land to create units for vertical or horizontal drilling. Lessee shall pool/unitize all of the Lessor's Land within a "Drilling Unit" if it exercises its said rights. The unit formed by such pooling for an oil well which is not a horizontal completion shall not exceed forty (40) acres plus a maximum acreage tolerance of ten percent (10%), and for a gas well or a horizontal completion shall not exceed 320 acres, provided that a larger unit may be formed for an oil well or gas well or horizontal completion with the Lessor's written consent, which shall not be unreasonably withheld. The failure of Lessor to object to Lessee's written proposal to create a larger unit within thirty (30) days of Lessor's receipt of said proposal will constitute approval of the same. A unit may be further increased in size to conform to any well spacing or density pattern that may be prescribed or permitted by any governmental authority having jurisdiction to do so. Pooled units shall only become effective when Lessee files in the Real Property Records of the county where the Land is located a document describing the unit acreage and depths for the unit and delivers a copy of the document to the Lessor. There shall be allocated to the Land included in the unit that prorated portion of the gas produced from the unit that the number of surface acres of the Land included in the unit bears to the total number of surface acres included in the unit. Royalties shall be computed on the portion of production allocated to the Land.

8. **Offset Wells.** For purposes of this Lease, an "offsetting well" is a well that is producing oil or gas from adjacent or nearby land and is draining the Land. If an offsetting well is completed and continues to produce, Lessee must, within sixty (60) days after the initial production from the offsetting well, commence operations for the drilling of an offset well on the Land, as would a reasonably prudent operator under similar circumstances, and must diligently pursue those operations to the horizon in which the offsetting well is producing, or at the option of Lessee: (i) execute and deliver to Lessor a release in recordable form of the acreage nearest to the offsetting well not included in a producing unit; or (ii) pay Lessor a monthly royalty equal to the royalty that would be payable under this Lease if the production from the offsetting well had come from the Land. In the event acreage is released pursuant to (i) above, the release will, if possible, cover a tract of a size and shape that will permit the drilling of a well to the producing formation and the creation of a proration unit surrounding the well in compliance with the field rules for the field in which the offsetting well is located, but if there are no field rules, in compliance with the statewide rules of the Railroad Commission of Texas. A producing well located within 330 feet of the Land will be conclusively presumed to be draining the Land.

9. **Secondary Recovery.** Lessee will not implement any repressuring, pressure maintenance, recycling, or secondary recovery operations without the prior written consent of Lessor.

10. **Equipment.** While Lessee is not in default under this Lease, and subject to other provisions of this Lease, Lessee will have the right at any time within six (6) months after the expiration of this Lease to remove all personal property placed by Lessee under the Land by drilling. If Lessee fails to do so within the permitted period, then at Lessor's option, all or any part of the personal property will become the property of Lessor, and Lessor may require Lessee to remove all property not desired by Lessor.

11. **No Surface Activities.** There is hereby accepted and reserved to LESSOR the full use of the land covered hereby and all rights with respect to the surface and subsurface thereof for any and all purposes and all minerals except those expressly leased herein and only to the extent herein leased to LESSEE. LESSOR reserves and accepts from this Lease all of the surface of the land described in paragraph 1, and LESSEE agrees that it will not conduct drilling operations or any other

operations or activities of any nature on the surface of such Land. Lessee its agents, contractors, heirs, successors or assigns shall have no rights of ingress or egress upon the surface of the Land and herein waives any rights to any implied easement to use the surface of the Land. Lessee shall not construct any pipelines on or under the Land by any means.

12. Assignments. Lessor is granting rights to Lessee that Lessor would not grant to others. Therefore, prior written approval of Lessor is required for any assignment or sublease of this Lease, other than to officers or affiliates of Lessee. Said written approval shall not be unreasonably withheld. All assignments and subleases must require the assignee or sublessee to assume all of Lessee's obligations under this Lease, but Lessee will remain liable for its obligations regardless of any assignment or sublease by it. No assignment or sublease will be effective until a certified copy of the recorded document is furnished to Lessor.

13. Force Majeure. Should Lessee be prevented by reason of Force Majeure from complying with any express or implied covenant of this Lease (other than a requirement to pay money), from conducting drilling or reworking operations on the Land, or from producing oil or gas, then while so prevented, that covenant will be suspended; Lessee will not be liable for damages for failure to comply therewith; this Lease will be extended so long as Lessee is prevented from conducting drilling or reworking operations on or from producing oil or gas from the Land; and the time while Lessee is so prevented will not be counted against Lessee. "Force Majeure" means any Act of God, any federal or state law, or any rule or regulation of governmental authority, or other similar cause (other than financial reasons). This paragraph is, however, in all things subject to the limitations of time during which this Lease may be continued in force by the payment of shut-in gas royalties.

14. No Warranties. Lessor makes no warranty of any kind with respect to title to the Land. By acceptance of this Lease, Lessee acknowledges that it has been given full opportunity to investigate and has conducted sufficient investigation to satisfy itself as to the title to the Land, and Lessee assumes all risk of title failures. If Lessor owns an interest in the Land less than the entire fee simple estate, then the royalties (including shut-in royalties) payable hereunder will be reduced proportionately. Lessee, at its option, may discharge any tax, mortgage, or other lien on the Land, and in the event Lessee does so, Lessee will have the option of applying the royalties accruing to Lessor toward payment of it.

15. Curing Defaults. Should Lessee at any time fail to comply with its obligations hereunder regarding construction, maintenance, or repair within thirty (30) days after written notice from Lessor, Lessor will have the right to do or have done whatever is necessary to fulfill the obligations to its satisfaction, and Lessee shall be liable to Lessor for the reasonable and necessary expenses thus incurred by Lessor, to be paid within ten (10) days after Lessor furnishes to Lessee an itemized written statement of the expenses.

16. Notices. All notices will be deemed given and reports will be deemed delivered if sent by certified letter, return receipt requested, properly addressed and deposited in the United States Postal Service, postage prepaid, to Lessor and Lessee at the addresses shown for each party. Any party may designate a new address by proper notice to the other party or parties.

17. Attorney's Fees. In the event that either party is required to employ legal counsel for the enforcement of any provision of this Lease and prevails by obtaining a final unappealable judgment, the prevailing party will be entitled to recover reasonable attorney's fees and expenses incurred.

18. Insurance. At all times while this Lease is in force, Lessee shall acquire and maintain insurance covering all of its operations on the Land, including any work performed on its behalf by contractors, subcontractors, and others, naming Lessor and related individuals and entities designated by Lessor as additional insureds. The policies shall include coverage for comprehensive general liability, for bodily injury and property damage, blowout and loss of well coverage, and coverage for any damage to the environment, including coverage for the cost of clean up and surface remediation. The coverage shall be in the minimum amount of \$5,000,000.00. Upon written request from Lessor, Lessee shall furnish a certificate from the issuing insurance company or companies evidencing the coverage or documentation of the ability of Lessee to self insure. Said insurance requirements may be met by a combination of self-insurance, primary and excess policies.

19. **INDEMNITY.** LESSEE AGREES TO INDEMNIFY AND HOLD HARMLESS LESSOR, AND LESSOR'S REPRESENTATIVES, SUCCESSORS, AND ASSIGNS AGAINST ALL EXPENSES, CLAIMS, DEMANDS, LIABILITIES, AND CAUSES OF ACTION OF ANY NATURE FOR INJURY TO OR DEATH OF PERSONS AND LOSS OR DAMAGE TO PROPERTY, INCLUDING, WITHOUT LIMITATION, REASONABLE ATTORNEY FEES, EXPERT FEES, AND COURT COSTS, CAUSED BY LESSEE'S OPERATIONS ON THE LAND OR LESSEE'S MARKETING OF PRODUCTION FROM THE LAND OR ANY VIOLATION OF ANY ENVIRONMENTAL REQUIREMENTS BY LESSEE. AS USED IN THIS PARAGRAPH, THE TERM "LESSEE" INCLUDES LESSEE, ITS AGENTS, EMPLOYEES, SERVANTS, CONTRACTORS, AND ANY OTHER PERSON ACTING UNDER ITS DIRECTION AND CONTROL, AND ITS INDEPENDENT CONTRACTORS. LESSEE'S INDEMNITY OBLIGATIONS SURVIVE THE TERMINATION OF THIS LEASE.

20. **Dispute Resolution.** In the event of a dispute under this Lease, the parties agree to attempt to resolve the dispute through good faith mediation to be held Dallas County, Texas.

21. **Miscellaneous Provisions.**

(a) In the event this Lease expires for any reason as to all or any part of the Land, Lessee shall, within sixty (60) days thereafter, furnish Lessor with a written, recordable release covering all of the Land or that portion of the Land to be released.

(b) Nothing in this Lease negates the usual implied covenants imposed upon Lessee.

(c) Lessee will conduct all operations hereunder in compliance with the rules of the Railroad Commission of Texas and federal and state environmental laws and regulations. Lessee will give Lessor at least five (5) days prior notice in writing before conducting drilling, recompletion, or reworking operations under the Land. Upon request by Lessor, Lessee shall furnish to Lessor copies of applications to drill, daily drilling reports, well tests, completion reports, plugging records, gas purchase contracts, and production reports. Lessor has the right, personally or by representative, at Lessor's risk, of access to the derrick floor to observe all operations on all wells drilled on the Land. Lessor will have the right to witness the taking of all logs and drill stem tests, and Lessee agrees to furnish Lessor with copies of all logs and surveys taken promptly after taking them. Lessee will divulge to Lessor correct information as requested by Lessor as to each well, the production therefrom, and such technical information as Lessee may acquire. Lessor has the right to be present when wells or tanks are gauged and production metered and has the right to examine all run tickets and to have full information as to production and runs and to receive copies of all run tickets upon request. All information furnished to Lessor shall be held as confidential.

(d) The terms "production" and "producing" mean production and producing in paying quantities. No obligation of Lessee to pay money under this Lease will be excused or delayed by reason of Force Majeure. Lessee's obligations to pay money under this Lease are to be performed in Dallas County, Texas. Paragraph headings are used in this Lease for convenience only and are not to be considered in the interpretation or construction of this Lease. The execution or ratification by Lessor of any division order, gas contract, or any other document will not alter any provision of this Lease unless the intent to do so is expressly stated in the document. Lessee agrees to furnish to Lessor a copy of each title opinion or report obtained by Lessee that covers all or any part of the Land together with a copy of each title curative document obtained by Lessee.

(e) Lessor shall have the right to inspect all records of Lessee relating to this Lease, operations conducted on the Lease, the sale and marketing of production from the Lease, and the payment of royalties, including the right to audit Lessee's books insofar as they relate to the foregoing on an annual basis.

(f) The land may presently have an agricultural or open space exemption for ad valorem tax purposes. If this Lease or Lessee's activities cause the imposition of rollback taxes, Lessee agrees to hold Lessor harmless from any and all of the additional taxes.

(g) **Compressor Stations.** Lessee shall not locate any compressor stations on the Land. Lessee shall not locate a compressor station within 200 feet of the Land. Any compressor stations within 201 feet to 500 feet of the Land shall be screened by solid fencing and trees (whether naturally occurring or planted by Lessee).

(h) This Lease is binding upon and for the benefit of Lessor, Lessee, and their respective heirs, personal representatives, successors, and assigns.

Executed and effective on the date first written above.

LESSOR:

HOUGHTON PROPERTIES, LTD.
A Texas Limited Partnership

By: **COMMERCE FIRST FINANCIAL, INC.**,
General Partner

By: Andrew Smith
Capacity: President

LESSEE:

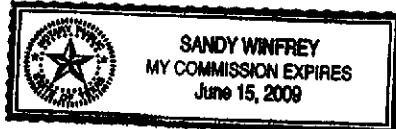
VARGAS ENERGY, LTD.
a Texas Limited Partnership
By Plover Production Company, LLC, its
sole General Partner

By: Crawford Edwards
Capacity: President

ACKNOWLEDGEMENTS

STATE OF TEXAS §
COUNTY OF Dallas §

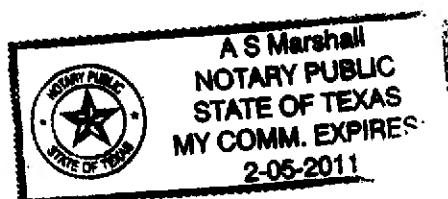
This instrument was acknowledged before me on this 5 day of Aug, 2008, by Andrew Smith as President of Commerce First Financial, Inc., the general partner of Houghton Properties, Ltd, a Texas Limited Partnership and on behalf of said limited partnership.



Sandy Winfrey
Notary Public, State of Texas
My Commission Expires: 6-15-08

STATE OF TX §
COUNTY OF Tarrant §

This instrument was acknowledged before me on this 20 day of Aug, 2008, by Crawford Edwards as President of Plover Production Company, LLC, the sole General Partner of Vargas Energy, Ltd, a Texas limited partnership for and on behalf of said partnership in the capacity stated therein.



A S Marshall
Notary Public, State of TX
My Commission Expires: 2-5-11